BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 646 (Sub-No. 3)

WAYBILL DATA RELEASED IN THREE-BENCHMARK RAIL RATE PROCEEDINGS

OPENING COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY

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Canadian Pacific Railway Company ("CPR") submits these Opening Comments regarding the Notice of Proposed Rulemaking ("NPRM") served in the above-captioned proceeding on April 2, 2010. The NPRM proposes to replace the current requirement, under the Three Benchmark methodology for small rate reasonableness cases, that "comparison group" movements be selected from the most recent Waybill Sample. Specifically, the Board proposes to permit parties to select their comparison group movements from four years of Waybill Sample data that correspond to the most recently published RSAM. *See* NPRM at 2. For the reasons set forth hereinafter, the proposed rule is unsupported and inconsistent with the stated objectives of the Three Benchmark methodology, and should not be adopted.

The NPRM suffers from three substantial flaws. First, the NPRM violates fundamental administrative law principles because it contains no discussion of the Board's rationale for proposing the changed rule. The inclusion of such an explanation is not optional – it is a statutory requirement. Without a meaningful articulation of the Board's reasoning, parties cannot comment effectively on the proposed rule. Second, the proposed rule would severely impair the accuracy of the Three Benchmark approach by permitting rate comparisons based

upon long-outdated movements. Recent studies – including those conducted and/or commissioned by the Board itself – demonstrate both that rates and costs fluctuate significantly over time, and that they do not necessarily move in tandem. The greater the time lag between a challenged rate and the rates in a comparison group, the less likely it is that the Three Benchmark methodology will produce rate reasonableness determinations that are consistent with current market conditions. Third, there does not appear to be any legitimate justification (based on a flaw in the existing rule) for adopting a methodological change that would further diminish the accuracy of rate determinations in Three Benchmark cases.

I. THE BOARD'S FAILURE TO ARTICULATE A RATIONALE FOR THE PROPOSED RULE VIOLATES THE APA.

The NPRM proposes a highly significant modification to the Three Benchmark methodology. The impact of the Board's proposal is illustrated by the following example:

If a Three Benchmark proceeding were filed today, the 2008 Waybill Sample (the most recent Waybill Sample) would be the sole source of comparison movements. The Board would compare the R/VC ratio for the challenged rate with R/VC ratios produced by movements that occurred during 2008 – two years ago. However, if the proposed rule were adopted, the Board would permit the use of comparison movements drawn from the Waybill Samples "for the four years that correspond with the most recently published RSAM figures." *Id.* Because the last published RSAM is for the four-year period 2004-2007,[1] the comparison group could therefore include movements from as long ago as 2004 – six years ago. Still worse, the 2008 Waybill Sample would not be an eligible source of comparison movements because the 2008 RSAM has not yet been published. Thus, the rule proposed in the NPRM would actually forbid parties from

[1] *See Simplified Standards for Rail Rate Cases – 2007 RSAM and R/VC$_{>180}$ Calculations*, Ex Parte No. 689 (served May 12, 2009).

using the most recent available Waybill Sample data in developing their comparison groups, while opening the door for "comparable" movements based on traffic that moved as long as six years ago.

The NPRM does not even hint at the Board's rationale for proposing such a substantial (and illogical) change in its regulations. For that reason, the NPRM violates the basic notice-and-comment requirements of the Administrative Procedure Act. Agencies are required to explain their reasoning for actions they propose to take, so that parties have a fair opportunity to evaluate and comment on that reasoning. Because the Board failed to offer any indication of its reasons for revising the Three Benchmark approach, the NPRM is invalid.

The NPRM begins by recounting the procedural history of the *Simplified Standards* rulemaking, including the Board's initial proposal to release only the most recent Waybill Sample for use in selecting comparison group movements, its announcement in the final rule that four years of Waybill Sample data corresponding to the most recent RSAM would be released, and the D.C. Circuit's decision vacating the four-year Waybill Sample provision of the final rule in *CSX Transp. v. STB*, 568 F.3d 236, 246-47 (D.C. Cir. 2009). *See* NPRM at 1-2. After recounting that history, the Board states, without explanation, that it "now proposes to release to the parties the unmasked Waybill Sample data of the defendant carrier for the 4 years that correspond with the most recently published RSAM figures." *Id.* at 2. The NPRM contains no discussion whatsoever of the Board's reasons for proposing this change.[2]

The Board's failure to provide "sufficient factual detail and rationale for the rule to permit interested parties to comment meaningfully" violates the APA. *Nat'l Elec. Mfrs. Ass'n v.*

[2] The NPRM's references to the *Simplified Standards* proceeding do not constitute a rationale for the current NPRM. The final *Simplified Standards* rule did not give any reason for changing the Board's original proposal that parties can select comparison group data only from the most recent Waybill Sample.

EPA, 99 F.3d 1170, 1172 (D.C. Cir. 1997) (internal quotation marks omitted). An agency cannot simply declare what it plans to do; rather, it "must disclose in detail the thinking that has animated the form of a proposed rule and the data upon which that rule is based." *HBO v. FCC*, 567 F.2d 9, 35 (D.C. Cir. 1977). The Board's regulations likewise require that notices of proposed Board rulemakings include "[a] discussion of why the rulemakings are needed and what they are intended to accomplish." 49 C.F.R. § 1110.3(c)(2). Here, the NPRM fails under both the statutory APA requirement and the Board's own regulations.[3]

The Board's failure to articulate its rationale for the proposed rule prejudices the ability of CPR (and other interested parties) to comment meaningfully on the NPRM. CPR is left to hypothesize about possible reasons the Board might have for adopting the proposed rule. The NPRM effectively denies interested parties the statutorily-guaranteed right to evaluate and comment on the agency's stated rationale.

II. THE PROPOSED RULE WOULD FURTHER IMPAIR THE ACCURACY OF RATE DETERMINATIONS IN THREE BENCHMARK CASES.

The Three Benchmark methodology is, in essence, a "rate comparison" approach. As the Board observed in *Simplified Standards*, "[t]he whole purpose of the Three Benchmark approach is to determine where the challenged rate falls in comparison to other similarly situated traffic." *Simplified Standards* at 80. But a traffic movement that occurred six years prior to the challenged movement is not "similarly situated" in any meaningful sense. Multiple studies – including those commissioned by the Board – have demonstrated that rates and costs fluctuate significantly over time. The older the data used for a Three Benchmark comparison group, the

[3] In addition, the NPRM does not contain any citation to the legal authority under which the rule is proposed. Both the Board's regulations and the APA require a reference to the legal authority under which a rule is proposed. *See* 5 U.S.C. § 553(b)(2); 49 C.F.R. § 1110.3(c)(7); *Global Van Lines v. ICC*, 714 F.2d 1290 (5th Cir. 1983).

less "comparable" that data is to current traffic. The NPRM's proposal to permit the use of movements that are as much as three to six years old would dramatically reduce the reliability of rate comparisons produced by the Three Benchmark approach. (This is particularly true in light of the Board's refusal to prescribe any mechanism for adjusting historical comparison movement data to current levels.)

In the dynamic rail marketplace, both the rates and the costs of participating carriers change significantly over time. A recent Board study showed that real revenue per ton-mile fell 33% in the six years between 1985 and 1991, and rose by more than 15% in the three years between 2004 and 2007.[4] Similarly, a GAO study has documented that real, inflation-adjusted rail rates generally declined from 1985 through 1998; increased in 1999; dropped again in 2000; and increased in 2001 and 2002.[5] More recently, the Christiansen Associates report commissioned by the Board found that rates rose from 2004 through 2008 and fell in 2009.[6]

As these studies show, there is substantial quantitative proof that railroad rates and costs fluctuate significantly over any given period of three to six years. Even more importantly for purposes of evaluating the Board's proposed new rule, the studies indicate that rates and costs do not necessarily rise and fall in tandem or proportionally. Indeed, the Christiansen report concluded that "revenue per ton-mile and marginal cost tend to move together, *but not in*

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[4] *See* Surface Transportation Board, Office of Economics, Environmental Analysis and Administration, Section of Economics, Study of Railroad Rates: 1985-2007, at 1-2 (Jan. 2009), *available at* http://www.stb.dot.gov/industry/1985-2007RailroadRateStudy.pdf.

[5] U.S. Government Accountability Office, Freight Railroads: Industry Health Has Improved, But Concerns about Competition and Capacity Should Be Addressed, GAO 07-94, at 11-12 (Oct. 2006), *available at* http://www.gao.gov/new.items/d0794.pdf.

[6] *See* Laurits R. Christiansen Associates, Inc., An Update to the Study of Competition in the U.S. Freight Railroad Industry, at i, 2-5 (Jan. 2010).

proportion or consistently."[7] For these reasons, the R/VC ratio for a movement that occurred four, five or even six years ago is not a reliable benchmark for determining the reasonableness of a current rail rate. The Board's proposal to jettison the existing rule requiring that comparable groups be based only on the most recent available Waybill Sample, in favor of permitting the use of much older Waybill Sample data, would seriously undermine the reliability of the Three Benchmark methodology and produce arbitrary outcomes.

The Board's proposal to permit the use of older Waybill Sample data in selecting a comparison group might be less problematic if the Board's procedures included some mechanism for adjusting historical data to reflect subsequent changes in rate and cost levels in the current marketplace. But the *Simplified Standards* decision refused to implement commenters' suggestion that the Board adopt such an adjustment. *Simplified Standards* at 84-85. While the Board has suggested that it might consider such adjustments as "other relevant evidence" if presented by a party in a Three Benchmark proceeding, in practice the Board has applied evidentiary rules that make it all but impossible to present evidence of changing rates and costs. *See, e.g., E.I. du Pont de Nemours & Co. v. CSX Transp., Inc.*, STB Docket No. 42100, slip op. at 15-16 (served June 27, 2008).[8] As a result, the NPRM's proposal to allow comparison movements that are three-to-six years old would almost certainly lead to apples-to-oranges comparisons, with no consideration of how market circumstances affecting the rates and costs for those movements may have changed over time. If the Board adheres to its policy of

[7] *Id.* at 4-2 (emphasis added); *see also id.* at 4-3.

[8] In *DuPont*, the Board refused to consider the defendant's evidence that comparison group rates and costs had increased significantly over time on the grounds that the resulting adjusted R/VC_{COMP} could not be considered unless the defendant also made corresponding adjustments to the RSAM and $R/VC_{>180}$ benchmarks. *Id.* at 16. That requirement, which would require adjustments to many hundreds of individual movements, all but ensures that no party will be able to put forward evidence to adjust historical revenues and costs to current levels.

refusing to allow adjustments to historical comparison group data (a policy that CPR continues to maintain is misguided),[9] it must ensure that comparison groups are drawn from the most recent Waybill Sample data available.

III. THERE DOES NOT APPEAR TO BE ANY LEGITIMATE JUSTIFICATION FOR THE PROPOSED RULE.

In adopting the Three Benchmark methodology, the Board stated that it "seeks to make its rail rate dispute resolution procedures more affordable and accessible to shippers of small and medium-size shipments, while simultaneously ensuring that the new guidelines do not result in arbitrary ratemaking." *Simplified Standards* (decision served September 5, 2007) at 4 (emphasis added). While acknowledging that its simplified methodologies "[do not] offer[ ] as much precision and degree of confidence as a Full-SAC analysis," the Board concluded that they were necessary to ensure that shippers with smaller rate disputes "have some forum for rate relief." *Id. at* 5.

Without waiving its objections to the Board's failure to articulate its rationale for adopting the proposed rule, CPR observes that the Board's proposal is not consistent with the stated objectives of the Three Benchmark methodology. Permitting the use of Waybill Sample data that is as much as six years old is certainly not necessary to make the Three Benchmark methodology "more affordable and accessible to shippers." To the contrary, expanding the universe of traffic movements from which comparison groups are drawn from one to four years

[9] CPR and several other railroads argued in the D.C. Circuit that the *Simplified Standards* rule was arbitrary and capricious because it did not include a provision to adjust historical Waybill Sample data to reflect current rates and costs. Final Brief of Railroad Petitioners at 13-30, *CSX Transp. et al. v. STB*, Nos. 07-1369 *et al.* (D.C. Cir. filed Feb. 18, 2009). The D.C. Circuit reserved ruling on that argument in light of its holding that the Board violated APA notice-and-comment procedures when adopting the final rule in *Simplified Standards for Rail Rate Cases*, STB Ex Parte No. 646 (Sub-No. 1) (served Sept. 5, 2007). *See CSX Transp. v. STB*, 568 F.3d 1076, 1083 (D.C. Cir. 2009).

would, if anything, complicate the selection process, generate disputes regarding the relevance of "stale" data, and increase the expense of litigating Three Benchmark cases. At the same time, as CPR demonstrates in Part II above, the introduction of such older traffic data is utterly inconsistent with the Board's stated goal of "ensuring that the [Three Benchmark approach does] not result in arbitrary ratemaking."

There is no evidence to suggest that the current rule mandating use of the most recent Waybill Sample in selecting a comparison group has proven to be problematic, or that parties need access to a broader set of Waybill Sample data in order to develop an appropriate comparison group. In particular, the Board's experience with Three Benchmark cases does not support a conclusion that one year's Waybill Sample is insufficient. To date the Board has decided only four cases under the Three Benchmark standard. Not one of those cases involved comparison groups based upon only a single year's Waybill Sample data. The three *DuPont v. CSXT* cases were decided before the D.C. Circuit vacated in part the *Simplified Standards* decision and restored the original one-year Waybill Sample rule. In the fourth case, *U.S. Magnesium, LLC v. Union Pacific Railroad Co.*, comparison group evidence was filed before the D.C. Circuit's ruling, and the parties subsequently elected to proceed on the basis of that evidence rather than submitting new comparison groups following the Court's decision. *See* Status Report, *U.S. Magnesium, LLC v. Union Pacific R.R. Co.*, STB Docket No. 42114 (filed Nov. 10, 2009). Having never decided a Three Benchmark case based upon comparison groups drawn from a single year's Waybill Sample data, the Board cannot credibly conclude that such a pool of data is not adequate.

Moreover, the Board already has taken steps to address potential concerns about the sufficiency of comparison group data. For example, the Board has suggested that the Waybill

Sample may not contain sufficient movements of toxic by inhalation ("TIH") traffic to permit parties to create robust comparison groups in cases challenging rates for TIH traffic. The Board has proposed to remedy that problem by changing the rules for waybill sample reporting to require railroads to include all waybill information for TIH movements. *See Waybill Data Reporting for Toxic Inhalation Hazards*, STB Ex Parte No. 385 (Sub-No. 7), (served Jan. 28, 2010) at 4. That proposal, if adopted, will resolve any concerns about having enough TIH traffic in a single year's Waybill Sample for use in a Three Benchmark case.[10]

In addition, *Simplified Standards* itself provides a mechanism for Three Benchmark cases to proceed if the most recent Waybill Sample does not contain a sufficient number of comparable movements. Specifically, the Board explained that "if the Waybill Sample contains no useful comparison traffic," it would "entertain a reasonably tailored request for comparable movements from the defendant's own traffic tapes." *Simplified Standards* at 83. There is no need for the Board to preemptively expand the pool of Waybill Sample data to be used in all cases when there is no evidence that the pool needs to be larger and where the current rules provide remedies in the event the pool proves to be too small in an individual case.

CONCLUSION

The Board's proposal to revive the "four-year Waybill Sample" provision of *Simplified Standards* that the D.C. Circuit struck down should not be adopted. There is no legitimate justification for adopting such a marked change to the Three Benchmark methodology. To the contrary, the proposed rule is flatly inconsistent with the Board's stated objectives in adopting

[10] The Association of American Railroads filed comments suggesting certain modifications to the Board's proposal in *Ex Parte 385 (Sub-No. 7)*. AAR's revisions would allow Three Benchmark litigants to have expanded access to TIH waybills, but would take steps to address security concerns with releasing such sensitive information. *See* Comments of the Association of American Railroads, STB Ex Parte No. 385 (Sub-No. 7) (filed Mar. 4, 2010).

the Three Benchmark approach, because it would seriously undermine the reliability of R/VC ratio comparisons produced by that methodology and generate arbitrary outcomes in Three Benchmark cases.

Respectfully submitted,

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